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Coeur d' Alene Trust
Asset Allocation Review

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Executive summary

Current equity allocation is reasonable, given the long time horizon of the trust and high annual payout of $25m in real terms

- When setting the strategic asset allocation, there are two components of risk to consider – the risk of losing money in the short-term (i.e. negative annual returns) and the risk of not being able to meet the spending commitments over the long-term
- While the higher volatility of equity increases the risk of losing money in the short-term, its higher expected return over the long-term increases the probability of being able to meet future spending commitments

As trust assets increase, less equity is needed to target the same expected life

- As a result of the lower volatility, the 10% downside life improves (i.e. probability of not running out of money), while the probability of lasting at least 50 years decreases

Due to long-term nature of the trust, a shift to 100% government bonds is not recommend

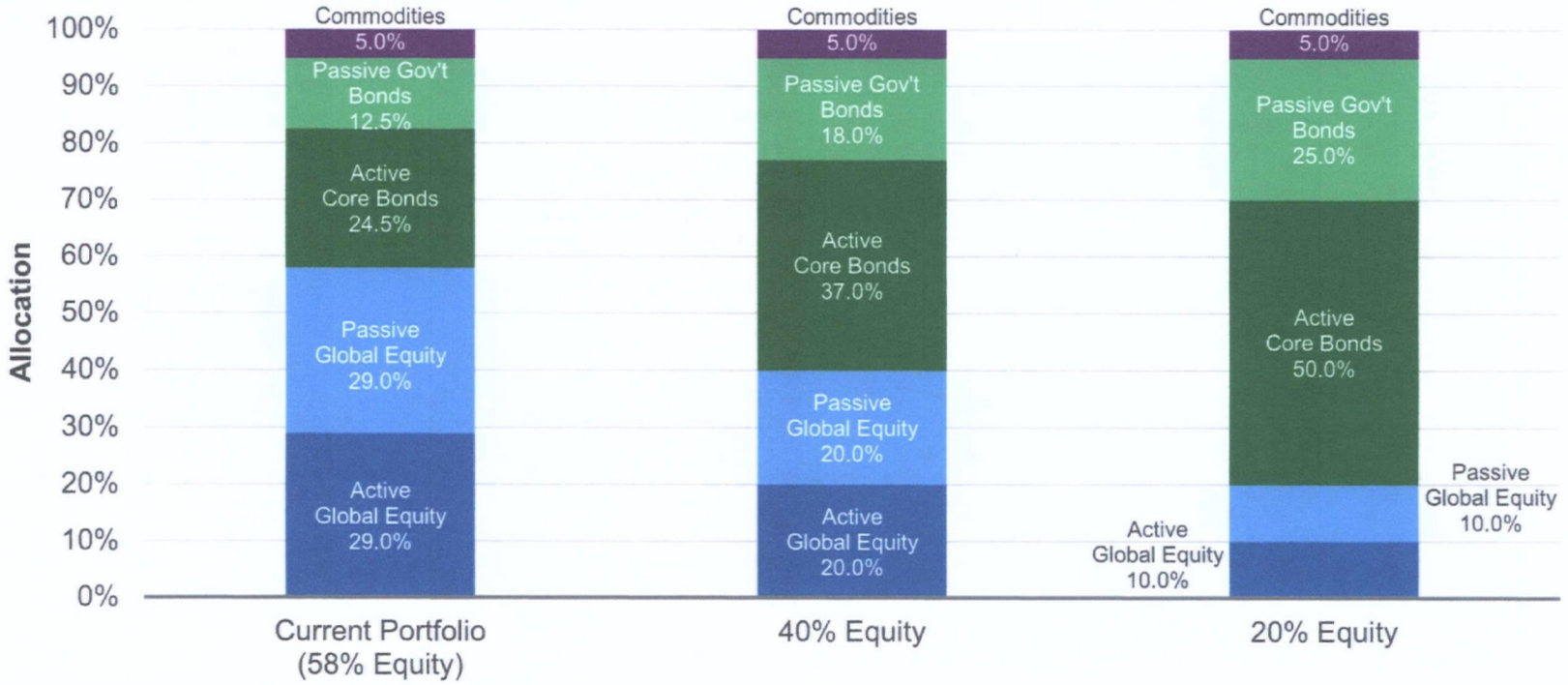
- Treasury real yield curve ends at 30 years, making it impossible to construct a portfolio that completely immunizes future spending commitments
  - $500m of inflation-linked bonds (TIPS) can guarantee approximately 21 years of spending, far short of the target 50+ years
  - ~$650M of inflation-linked bonds (TIPS) only guarantees 30 years of spending, also far short of the target 50+ years

Current investment strategy is constructed using a *Total Return* framework, resulting in a well-diversified portfolio seeking income *and* capital appreciation

- Income only focus leads to concentrated portfolios with considerable idiosyncratic risk

Effect of equity allocation on trust life

Overview of the current and alternative portfolios



	Current Portfolio	40% Equity	20% Equity
Expected Life	44 yrs	36 yrs	30 yrs
10% Downside Life	23 yrs	23 yrs	23 yrs
Prob. Lasting 50+ yrs	43%	25%	3%

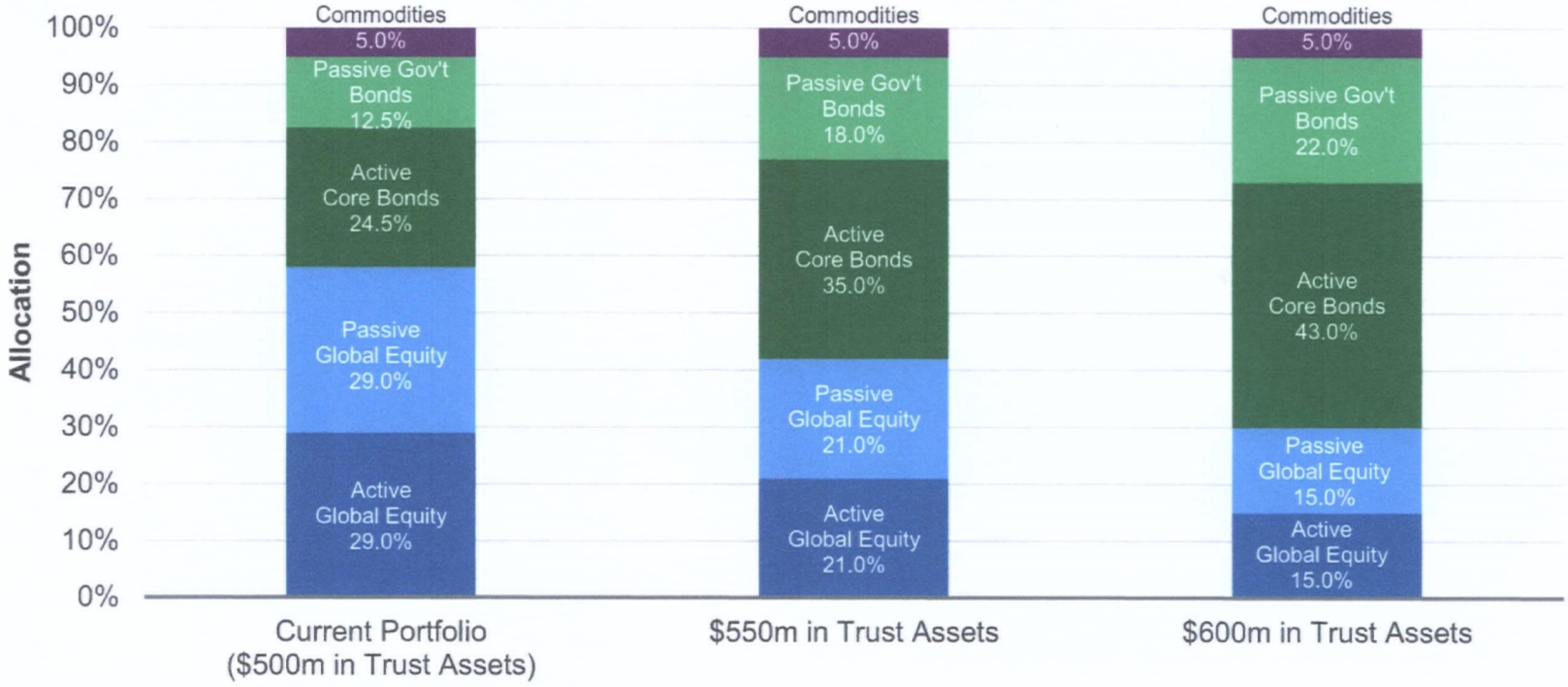
Equities increase the expected life of the trust, while providing a similar level of downside risk as the portfolios with more bonds

- Although equities are more risky than bonds in the short-term, they have a higher expected return over long time horizons and provide growth to help meet the $25m annual spending obligation (in real terms)

Source: BlackRock. See Appendix for long-term capital market assumptions.

Effect of trust size on required equity allocation

Overview of the current and alternative portfolios



	Current Portfolio	$550m in Trust Assets	$600m in Trust Assets
Expected Life	44 yrs	44 yrs	44 yrs
10% Downside Life	23 yrs	26 yrs	30 yrs
Prob. Lasting 50+ yrs	43%	40%	37%
Equity Allocation	58%	42%	30%

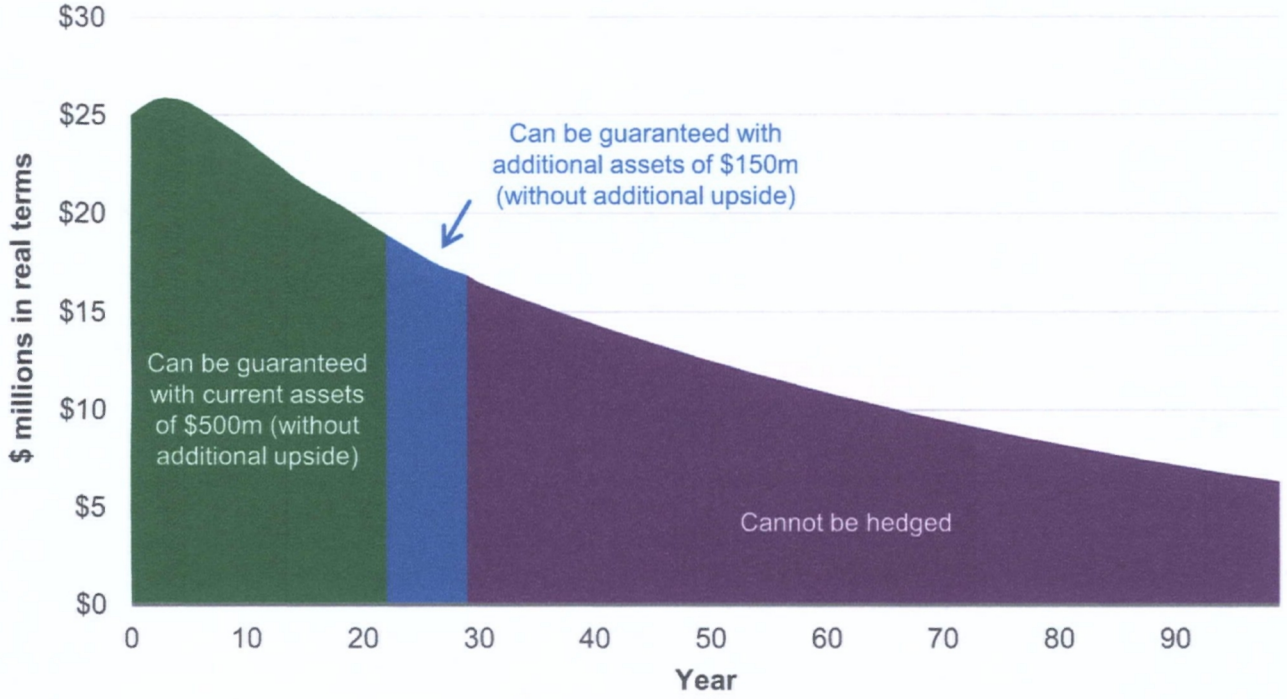
As the size of the trust increases, a smaller allocation to equities is needed to reach the same expected life

- As a result of the lower volatility, the 10% downside life improves, while the probability of lasting at least 50 years decreases

Source: BlackRock. See Appendix for long-term capital market assumptions.

How large does the trust have to be in order to allocate 100% of the capital to government bonds?

Present value of annual spending



If the trust is willing to sacrifice all upside potential, it is possible to guarantee annual real spending of $25m for approximately 21 years by purchasing inflation-linked bonds (TIPS)

- This is not recommended – the 21 year life is less than the 10% downside life of 23 years for the current and alternative portfolios

If the trust were ~$150m larger ($650m), it would be possible to guarantee spending for 30 years

- As before, this sacrifices upside potential and would not be recommended

Source: BlackRock, BofA ML.

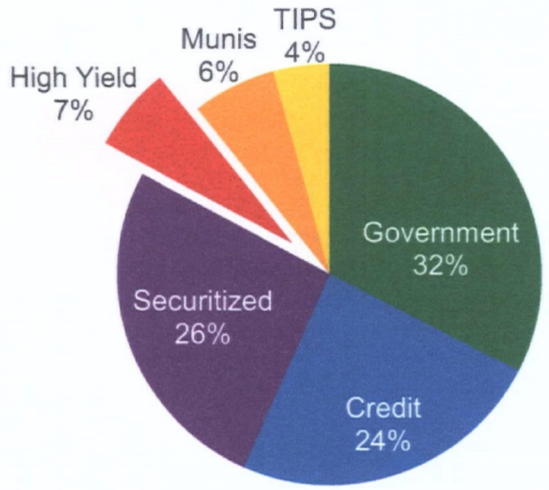
Why think in terms of total return instead of income?

Thinking in terms of income causes investors to construct concentrated portfolios

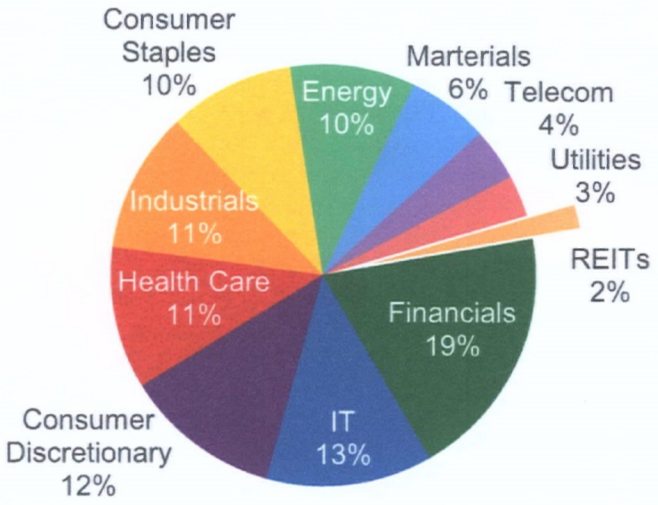
- Investors would likely allocation heavily to high yield within the bond allocation and to REITs within the equity allocation
- High yield and REITs are only 7% and 2%, respectively, of their security universes, introducing significant idiosyncratic risk relative to a well diversified portfolio

Potential risks	
High yield	**REITs** real estate investment trusts
▸ If income isn't reinvested, capital will erode over time as companies default on debt ▸ Adds considerably more credit risk than investment grade bonds, which is highly correlated with equity markets ▸ Doesn't add significant interest rate risk, which is diversifying at a total portfolio level	▸ During deflationary environments, returns will be poor due to losses from both property values falling and the real value of the debt used to finance purchases increasing ▸ Due to tax laws, REITs must distribute earnings, leading to limited capital growth if income isn't reinvested

High yield vs. US bond universe



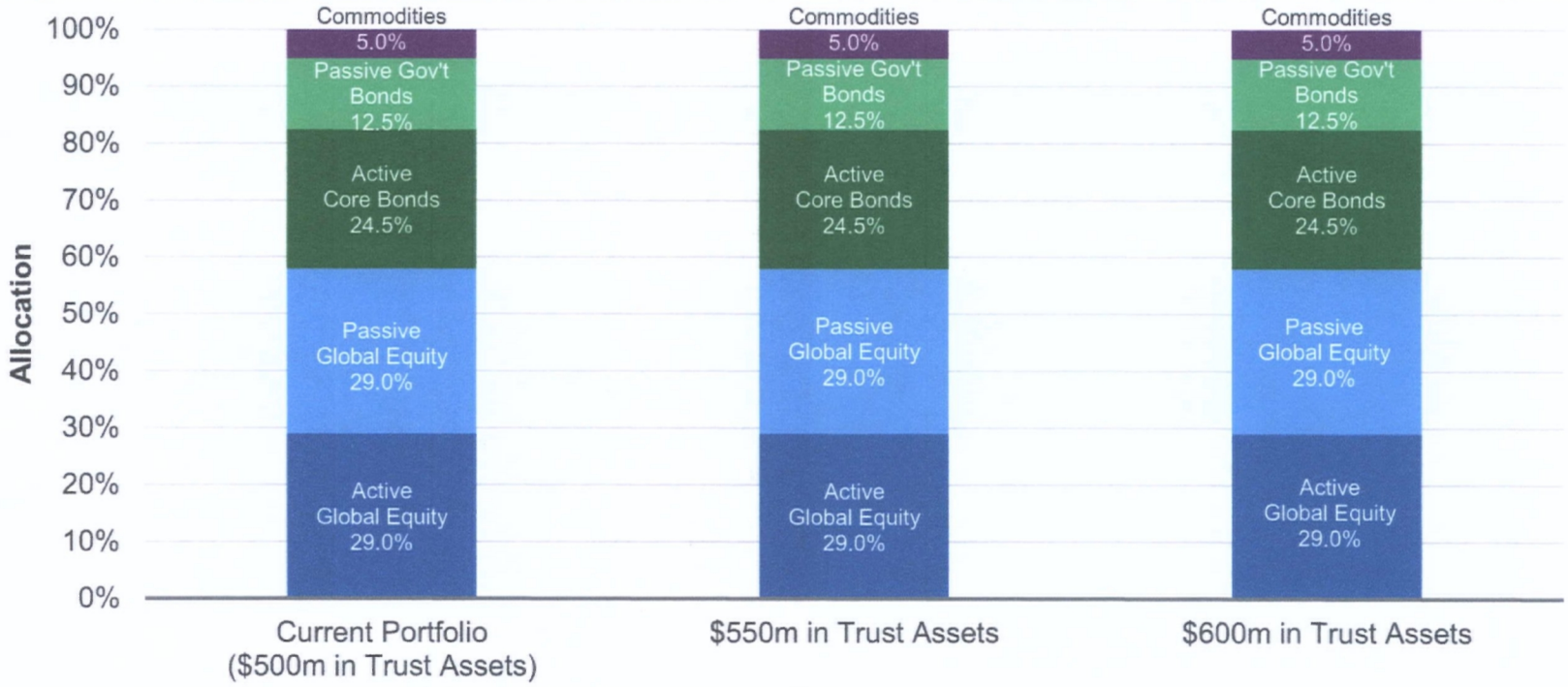
REITs vs. global equity universe



Source: BlackRock, MSCI, Barclays. As of February 28, 2014. US bond universe ignores small sectors that are not part of the Barclays US Aggregate Index, such as 144A securities, convertible bonds, etc.

Appendix A – Effect of trust size on the current policy allocation

Overview of the current portfolio at different sizes



	Current Portfolio	$550m in Trust Assets	$600m in Trust Assets
Expected Life	44 yrs	55 yrs	72 yrs
10% Downside Life	23 yrs	26 yrs	29 yrs
Prob. Lasting 50+ yrs	43%	53%	63%

Source: BlackRock. See Appendix for long-term capital market assumptions.

Appendix B – BlackRock's long-term capital market assumptions

Asset Class	Expected Return	Expected Volatility
US Equities	7.25%	17.00%
Int'l Dev Equities	7.25%	18.00%
EM Equities	9.00%	26.00%
US Core Bonds	3.00%	4.50%
US Govt Bonds	2.75%	4.00%
Commodities	2.75%	24.00%
Cash	1.75%	1.50%
Inflation	2.25%	

Expected Correlations	US Equities	Int'l Dev Equities	EM Equities	US Core Bonds	US Govt Bonds	Comm-odities	Cash
US Equities	1.00						
Int'l Dev Equities	0.85	1.00					
EM Equities	0.80	0.80	1.00				
US Core Bonds	0.10	0.10	0.10	1.00			
US Govt Bonds	0.15	0.10	0.10	0.90	1.00		
Commodities	0.25	0.25	0.30	0.00	0.00	1.00	
Cash	0.00	0.00	0.00	0.00	0.00	0.00	1.00

Expected Alpha Correlations	ACWI Alpha Tilts	Global Multi-Cap Equities	Core Active
ACWI Alpha Tilts	1.00		
Global Multi-Cap Equities	0.00	1.00	
Core Active	0.00	0.00	1.00

Strategy	Expected Alpha	Expexted Active Risk	Fee
ACWI Alpha Tilts	1.75%	2.00%	0.45%
Global Multi-Cap Equities	3.00%	6.00%	0.60%
Core Active	0.50%	0.75%	0.15%
MSCI ACWI IMI Index			0.09%
U.S. Government Bond Index			0.03%
S&P GSCI™ Commodities			0.25%